Visa Business and Economic Insights

U.S. Economic Outlook

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A tale of two economies: manufacturing vs. services

In this month's update, we extend our forecast horizon through the end of 2021. Thematically, growth is expected to begin downshifting but remain positive heading into 2020 and beyond. Ongoing trade tensions will likely remain unresolved over the forecast horizon and thus weigh on global growth. Soft global growth could have three main effects on the U.S. economy. First, continued pressure on export activity along with modest domestic demand, translating into slower growth from net exports. Second, weakness in the manufacturing sector for the foreseeable future that holds back business fixed investment. Finally, foreign capital inflows into the U.S., likely keeping longer-term interest rates lower and the dollar stable over the coming quarters.

The result will be a continuation of the tale of two economies, with manufacturing struggling while the services side of the economy continues to expand. Overall, the slow global growth and trade-related headwinds combine to push growth below 2 percent in 2020, with a further deceleration in 2021. The U.S. consumer will be the key support to growth over the next couple of years as fundamentals such as job growth and wage gains still support modest real consumption growth between 2.0-2.5 percent.

Key Takeaways

Divergence between manufacturing and services

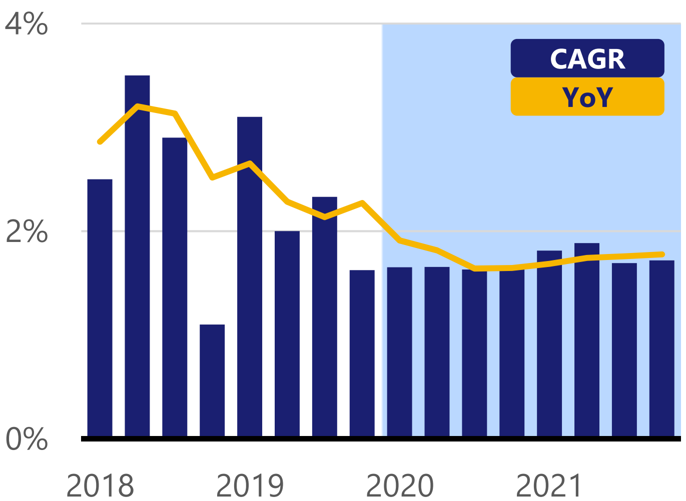
GDP growth to gradually downshift

Consumer fundamentals remain solid

Beware of negative headlines impacting confidence

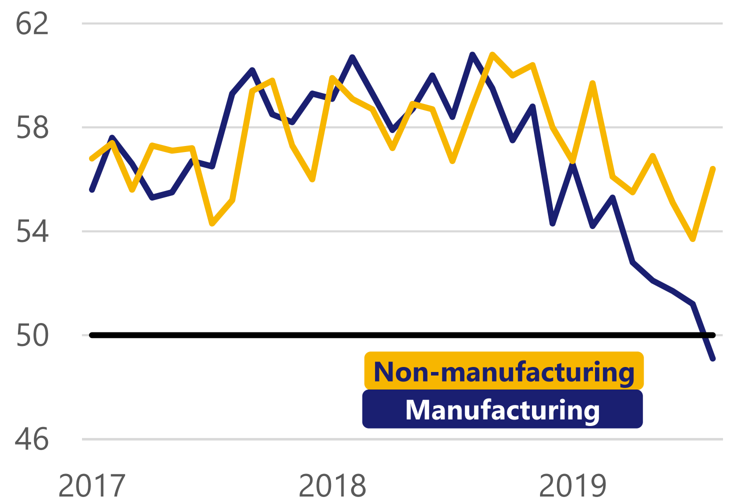
Real gross domestic product
(SA, CAGR and YoY percent change*)

Last forecast: September 2019



ISM Manufacturing vs. Non-Manufacturing Index
(Index, expansion: >50, contraction: <50)

Last actual: August 2019



Source: Visa Business and Economic Insights, U.S. Department of Commerce and Federal Reserve Board. * SA: seasonally adjusted, CAGR: compound annual growth rate, YoY: year-over-year.

A tale of two economies: manufacturing vs. services (cont.)

Confidence is key

The number of jobs created last month was disappointing, but August's employment report was not surprising given that the U.S. is simply running out of individuals to hire. Fundamentals behind consumer spending remain solid. While job gains have slowed, the trend in average hours worked (a leading indicator) remains positive and suggests further momentum behind wage growth. Real spending is expected to rise 3.5 percent in the third quarter before downshifting to 2.5 percent in Q4. Waning confidence and slower income growth in 2020 will likely keep real spending within the range of 2.3-2.4 percent on a quarterly basis in 2020. Nominal spending is likely to pick up in 2020 due to higher inflation rates.

The future path of interest rates

The Fed is likely to cut rates once again during its meeting later this month and thereafter leave rates unchanged for the foreseeable future unless economic conditions begin to deteriorate beyond the general slower growth we are projecting. The outlook for other interest rates is the subject of considerable uncertainty. With the next rate cut from the Fed, we suspect that the yield curve will begin to steepen a bit, which will likely elevate concerns about tighter credit conditions.

That said, longer-term interest rates are driven more by global factors and thus could swing wildly depending on economic data and central bank actions from abroad.

Key risks to the outlook

With consumer spending serving as the only solid support to economic growth (and most important at roughly 70 percent of GDP growth as of Q2), the U.S. economy remains vulnerable to any shock to consumer confidence. It just takes a few days of an equity market sell-off or negative headlines for consumer confidence—and, in turn real consumer spending—to falter. The other key area of concern is the manufacturing sector, which is on the cusp of its own recession. While hiring activity in the sector remains positive, further escalations in trade tensions and/or slower global economic growth conditions could combine to create even more downside risk to those parts of the country dependent on manufacturing. In addition, it is also possible that consumer prices will begin to climb as a result of the recent round of tariffs on China (some starting this month, with another round scheduled in December). Finally, should a resolution to the ongoing trade tensions occur, there would likely be some upward revisions to our growth outlook and downside risk to our inflation forecast.

Visa's U.S. Economic Forecast

	Actual		Forecast						Actual	Forecast		
	2019				2020				2018	2019	2020	2021
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Gross Domestic Product (CAGR)	3.1	2.0	2.3	1.6	1.7	1.7	1.6	1.6	2.9	2.3	1.8	1.7
Personal Consumption	1.1	4.7	3.5	2.5	2.4	2.4	2.3	2.3	3.0	2.7	2.7	2.2
Business Fixed Investment	4.4	-0.6	-0.8	-0.7	-0.2	0.3	0.8	1.2	6.4	2.4	-0.1	1.4
Equipment	-0.1	0.7	-3.5	-2.5	-2.0	-1.0	0.0	0.5	6.8	1.4	-1.5	0.6
Intellectual Property Products	10.8	3.7	5.0	4.0	3.8	3.8	3.6	3.6	7.4	7.6	3.9	3.5
Structures	4.0	-9.4	-7.5	-5.0	-3.5	-3.0	-2.5	-2.0	4.1	-3.5	-4.4	-0.9
Residential Construction	-1.0	-2.9	0.5	1.8	1.5	1.8	2.0	2.0	-1.5	-2.3	1.3	1.8
Government Purchases	2.9	4.5	1.5	1.8	1.3	1.3	1.1	1.1	1.7	2.2	1.6	1.1
Net Exports Contribution to Growth (%)	0.7	-0.7	-0.4	-0.3	-0.2	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.2
Inventory Change Contribution to Growth (%)	0.5	-0.9	0.0	-0.1	0.0	-0.1	0.0	-0.1	0.1	0.2	-0.1	0.0
Nominal Personal Consumption (YoY % Chg.)	3.9	4.1	4.3	4.8	5.3	4.7	4.5	4.4	5.2	4.3	4.7	4.0
Nominal Personal Income	4.6	4.9	4.7	5.0	4.4	3.7	3.9	4.0	5.6	4.8	4.0	3.9
Retail Sales Ex-Autos	3.0	3.4	4.1	5.3	5.6	4.8	4.0	4.1	5.5	4.0	4.6	3.7
Consumer Price Index	1.6	1.8	1.9	2.5	2.5	2.0	2.2	2.3	2.4	2.0	2.2	2.3
Federal Funds Rate (Upper Bound)	2.50	2.50	2.00	2.00	2.00	2.00	2.00	2.00	2.13	2.25	2.00	2.00
Prime Rate	5.50	5.50	5.00	5.00	5.00	5.00	5.00	5.00	4.90	5.25	5.00	5.00
10-Year Treasury Yield	2.41	2.00	1.60	1.63	1.68	1.73	1.76	1.78	2.91	1.91	1.74	1.82

Sources: Visa Business and Economic Insights analysis of data from the U.S. Department of Commerce, U.S. Department of Labor and Federal Reserve Board

Forward Looking Statements

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